

Message Text

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R 090711Z FEB 76

FM AMEMBASSY BUCHAREST

TO SECSTATE WASHDC 6554

INFO USDOC WSHDC

TREASURY WASHDC

AMEMBASSY BERLIN

AMEMBASSY BUDAPEST

AMEMBASSY MOSCOW

AMEMBASSY PRAGUE

AMEMBASSY SOFIA

AMEMBASSY WARSAW

USLO PEKING

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E.O. 11652: N/A

TAGS: EEWT, XH, RO

SUBJ: EAST-WEST FOREIGN TRADE BOARD STUDY OF COMPENSATION

ARRANGEMENTS: ROMANIA

REF: STATE 012648, MOSCOW 1106

1. SUMMARY: ALTHOUGH THE USE OF COMPENSATION ARRANGEMENTS IN ROMANIA'S TRADE HAS MUCH IN COMMON WITH THAT OF THE SOVIET UNION, AS DESCRIBED IN MOSCOW 1106, THE SCALE AND VARIETY OF SUCH OPERATIONS IS SO DIFFERENT IN ROMANIA THAT THE EMBASSY FEELS SEPARATE COMMENTS ARE NECESSARY.

2. FOLLOWING COMMENTS ARE BASED ON FORMAT SUPPLIED STATE
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012648.

I. TYPES OF COMPENSATION ARRANGEMENTS. EMBASSY IS AWARE OF FOUR TYPES OF NON-MONETARY COMPENSATION IN ROMANIAN TRADE, NOT INCLUDING COMBINATIONS.

(A) BARTER. SOME COMMODITY TRADE INVOLVES A SIMPLE EXCHANGE OF GOODS, WITH OR WITHOUT A CASH PAYMENT TO MAKE UP ANY DIFFERENCE IN VALUE. IN CHEMICALS, FOR EXAMPLE, THE EXCHANGE MAY BE BASED ON A SIMPLE RATION OF ONE PRODUCT TO THE OTHER; WE UNDERSTAND THAT IN SOME CASES THE CONTRACT DOES NOT EVEN PRESCRIBE A PRICE VALUE. SUCH DEALS DO NOT GENERALLY INVOLVE GOVERNMENT FINANCE OF ANY KIND, AND THE GOODS EXCHANGED ARE OFTEN CLOSELY RELATED PRODUCTS.

(B) COMPENSATION PAYMENTS FOR IMPORTED GOODS, NOT NECESSARILY IN RELATED PRODUCTS. FOR FOREIGN TRADE ORGANIZATIONS OFTEN REQUIRE FOREIGN SUPPLIERS TO TAKE BACK ROMANIAN PRODUCTS, ESPECIALLY IF THE FOREIGN GOODS DO NOT ENJOY A HIGH PRIORITY FOR ROMANIAN FOREIGN EXCHANGE. FOR EXAMPLE, A SELLER OF DENTAL OR HOSPITAL EQUIPMENT MIGHT BE ASKED TO BUY ROMANIAN MARMALADE. MORE TYPICALLY, A FOREIGN TRADE ORGANIZATION WOULD SEEK TO UNLOAD ON THE FOREIGN SUPPLIER PRODUCTS HANDLED BY THE SAME ORGANIZATION OR AT LEAST BY THE ORGANIZATION'S MINISTRY. THIS CAN ALSO HAPPEN WHEN PROPOSED SALES TO ROMANIA ARE FOR HIGH PRIORITY IMPORTS BUT THERE IS SUBSTANTIAL INTERNATIONAL COMPETITION. FOR EXAMPLE, A SUPPLIER OF PETROCHEMICAL TECHNOLOGY MIGHT BE ASKED TO BUY CERTAIN PETRO-CHEMICALS ALREADY IN PRODUCTION WHICH ROMANIA MAY BE ANXIOUS TO MARKET.

(C) BUY-BACK OF PRODUCTS RESULTING FROM CAPITAL EQUIPMENT OR TECHNOLOGY SALES. THIS TYPE USUALLY REFLECTS ACTIVE INTERNATIONAL COMPETITION, ESPECIALLY FOR SALES OF COMPLETE PLANTS, AND IS SIMILAR TO SOVIET ARRANGEMENTS DESCRIBED MOSCOW 1106, ALTHOUGH EACH DEAL IS USUALLY ON A MUCH SMALLER SCALE. LESS OFTEN IT MAY REPRESENT AN EFFORT OF FOREIGN FIRM TO OBTAIN A NEW SOURCE OF SUPPLY.

(D) JOINT VENTURE MARKETING. FORMATION OF A JOINT VENTURE IN ROMANIA USUALLY COMMITS THE FOREIGN PARTNER TO MARKET A LIMITED OFFICIAL USE

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LARGE SHARE OF THE JOINT VENTURE'S PRODUCTS OVERSEAS, ONCE THE PLANT IS IN OPERATION, WHETHER OR NOT THIS REPRESENTS ANY FORM OF COMPENSATION FOR THE FOREIGN PARTNERS' INVESTMENT. FOR EXPECTS EACH JOINT VENTURE TO EARN ENOUGH FOREIGN EXCHANGE TO COVER ALL ITS FOREIGN EXCHANGE COSTS INCLUDING POTENTIAL PROFITS; MOREOVER, THE ADVICE, ASSISTANCE AND EXAMPLE OF A FOREIGN FIRM WITH MARKETING EXPERIENCE IN THE FIELD IS OFTEN A PRIMARY INCENTIVE TO FOR TO CONSIDER ESTAB-

LISHING A JOINT VENTURE AT ALL. THE FOREIGN PARTNER ALSO HAS AN EQUITY INTEREST IN THE PROFITABILITY (AND THEREFORE THE MARKETING SUCCESS) OF HIS INVESTMENT.

II. SIMILARITIES/DIFFERENCES TO TRADITIONAL FOREIGN INVESTMENT. GENERALLY SPEAKING, FIRMS WHICH AGREE TO COMPENSATION ARRANGEMENTS IN ROMANIA DO NOT THINK OF THEM AS A RETURN ON INVESTMENT, BUT RATHER AS A FORM OF PAYMENT FOR A SALE. IF THE COMPENSATION IS DEFERRED, THEY THEN NEED TO FINANCE IT. IN THE CASE OF TYPE I (D) ABOVE, WHERE MARKETING IS UNDERTAKEN FOR A JOINT VENTURE IN WHICH THE FOREIGN FIRM HAS AN EQUITY INVESTMENT, THE MARKETING IS INDIRECTLY LINKED TO ITS RETURN ON INVESTMENT: THE FOREIGN FIRM'S RETURN ON INVESTMENT SHOULD FLOW DIRECTLY FROM THE JOINT VENTURE ITSELF. MOST COMPENSATION ARRANGEMENTS ARE THUS A FORM OF SUPPORT FOR A JOINT VENTURE OR A SALE, NOT DIRECT SOURCE OF PROFIT, ALTHOUGH A PROJECT SPECIFICALLY DESIGNED TO INCREASE A FOREIGN FIRM'S SUPPLY COULD BE SUCH A SOURCE.

III. SIGNIFICANCE OF COMPENSATION ARRANGEMENTS. ROMANIAN FOREIGN TRADE ORGANIZATIONS ALWAYS ASK FOR COMPENSATION IN PRODUCTS; WHETHER THEY GET IT DEPENDS UPON THE COMPETITIVE SITUATION. ALTHOUGH WE HAVE NO VALUE DATA, WE ARE CERTAIN THAT COMPENSATION ARRANGEMENTS ARE INVOLVED IN A SUBSTANTIAL PART OF ROMANIAN TRADE WITH THE WEST, EVEN THOUGH THE COMPENSATION IS NOT ALWAYS A LARGE PART OF ANY ONE DEAL. IN SOME CASES WE SUSPECT THAT AGREEMENT TO ACCEPT COMPENSATION IN GOODS MAY BE MORE A TOKEN OF THE FOREIGN FIRM'S WILLINGNESS TO COMPROMISE WITH GOVERNMENT OBJECTIVES THAN IT IS A QUANTITATIVELY SIGNIFICANT ASPECT OF THE DEAL. COMPENSATION IS LESS FREQUENTLY ACCEPTED BY U.S. FIRMS, IN PART BECAUSE MANY COMING TO ROMANIA ARE SELLING HIGH (OR PERHAPS UNIQUE) TECHNOLOGY; BUT THIS MAY ALSO EXPLAIN THE RATHER POOR RECORD OF U.S. FIRMS IN COMPETING FOR LIMITED OFFICIAL USE

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WITH WEST EUROPEAN AND JAPANESE SUPPLIERS OF STANDARD CAPITAL GOODS IN THIS MARKET. CONSUMER GOODS SOLD ON THE ROMANIAN DOMESTIC MARKET ARE PURCHASED ONLY UNDER BARTER TERMS: THE SUPPLIER MUST ACCEPT ROMANIAN GOODS FOR 100 PERCENT OF HIS PAYMENT. CONSEQUENTLY NO U.S. CONSUMER GOODS ARE AVAILABLE ON THE ROMANIAN DOMESTIC MARKET.

IV. IMPACT ON TRADE OF COMPENSATION ARRANGEMENTS.

(A) SHORT TERM. WHEN U.S. FIRMS FEEL THEY MUST ACCEPT SHORT-TERM COMPENSATION ARRANGEMENTS IN ROMANIA, THEY MUST THEN FIND OUTLETS FOR OFTEN UNRELATED PRODUCTS. SOME FIRMS HAVE SUCCESSFULLY USED EUROPEAN TRADING COMPANIES FOR THIS PURPOSE, OTHERS HAVE DONE THE TRADING THEMSELVES, WITH MIXED RESULTS. LACK OF U.S. EXPERIENCE IN THIS AREA REMAINS AN INHIBITING

FACTOR FOR U.S. EXPORTS.

(B) LONG TERM. COMPANIES WHICH UNDERTAKE LONG TERM COMMITMENTS, ESPECIALLY FOR MARKETING THE OUTPUT OF JOINT VENTURES, MAY NEED TO ESTABLISH ADDITIONAL SALES FACILITIES JUST TO SERVICE EXPORTS FROM THEIR JOINT VENTURE. THE PRINCIPAL EFFECT IS TO INCREASE ROMANIA'S EXPORTS AND EXPORT POTENTIAL.

(C) CHANGES IN TRADE. ALTHOUGH EVIDENCE IS LIMITED SO FAR, IN THE CASE OF LONG-TERM ARRANGEMENTS WITH FOREIGN FIRMS

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PERHAPS ROMANIA WILL LEARN ENOUGH ABOUT MARKETING ITS PRODUCTS ABROAD TO BE ABLE TO GRADUALLY ABANDON THE CRUTCH OF COMPENSATION ARRANGEMENTS, WHICH USUALLY ADDS TO THE COST

OF THEIR HARD-CURRENCY IMPORTS. LONG TERM LICENSING AND JOINT VENTURE MANUFACTURING ARRANGEMENTS PROVIDE THE BEST EXAMPLES OF CASES IN WHICH QUALITY STANDARDS HAVE BEEN RAISED TO MEET FOREIGN MARKETING REQUIREMENTS; THIS RESULTS DIRECTLY FROM THE FOREIGN PARTNERS' PARTICIPATION AND CONTRACT TERMS. THE ONE U.S. JOINT VENTURE SO FAR HAS ALSO OFFERED TO USE LOCAL CURRENCY MORE EFFECTIVELY BY ENGAGING IN TRIANGULAR TRADE WITH USSR AND WESTERN EUROPE.

V. ECONOMIC EFFECTS IN THE U.S.
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(A) IMPACT ON U.S. INDUSTRY AND JOBS. IN MOST CASES ROMANIAN PRODUCTS ACQUIRED UNDER COMPENSATION ARRANGEMENTS ARE NOT SOLD IN THE UNITED STATES, EITHER DUE TO POOR QUALITY, TRANSPORT COSTS, OR PERHAPS THE CONVENIENCE OF EUROPEAN TRADING FIRMS WHO MAY ACQUIRE TITLE TO THE GOODS. U.S. FIRMS ACCEPTING COMMODITIES (SUCH AS CHEMICALS) FOR THEIR OWN USE OFTEN DIRECT THEM TO OVERSEAS SUBSIDIARIES. NOW THAT BOTH MFN AND GSP TARIFF RATES APPLY TO U.S. IMPORTS FOR ROMANIA THIS SITUATION MAY CHANGE, BUT WE WOULD EXPECT THAT THE U.S. MARKET WILL BE TOO COMPETITIVE TO SOAK UP SUBSTANDARD ROMANIAN CONSUMER GOODS. TO THE EXTENT THAT U.S. INDUSTRY IS CHALLENGED AT ALL BY ROMANIA, IT WILL BE BY GOODS WHICH CAN BE EXPORTED FOR HARD CURRENCY, AND WE WOULD EXPECT THE BULK OF PRODUCTS EXPORTED AS COMPENSATION TO CONTINUE TO FLOW TO THE THIRD WORLD OR WESTERN EUROPE.

(B) EFFECTS ON U.S. EXPORTS TO THIRD COUNTRIES. EMBASSY IS NOT AWARE OF ANY COMPEITION BETWEEN ROMANIAN GOODS EXPORTED AS COMPENSATION AND U.S. EXPORTS. MOST MANUFACTURED GOODS SOLD BY ROMANIA ARE NOT GENERALLY EXPORTED BY THE U.S. CURRENT ROMANIAN PRODUCTS WHICH CAN COMPETE WITH U.S. EXPORTS ARE, ALMOST BY DEFINITION, EXCLUDED FROM ROUTINE IMPORT COMPENSATION ARRANGEMENTS. FOREIGN TRADE ORGANIZATIONS SEEK TO MARKET SUCH GOODS DIRECTLY. COMPENSATION FROM FUTURE PRODUCTION MIGHT OF COURSE CREATE A NEW SITUATION.

VI. MOTIVATION.

(A) SOCIALIST COUNTRIES. (1 AND 2). ROMANIA'S MOTIVATION FOR COMPENSATION THROUGH PRODUCTS REFLECTS ITS SHORTAGE OF HARD CURRENCY AND ITS INABILITY TO MARKET CERTAIN GOODS, EITHER BECAUSE OF LOW QUALITY OR LACK OF MARKETING SKILLS. SOMETIMES IT ALSO REFLECTS FAILURES IN THE PLANNING PROCESS WHICH PRODUCE SURPLUSES THAT CANNOT BE LIQUIDATED ANY OTHER WAY. WHEN THE GOODS CAN BE MARKETING FOR HARD CURRENCY, FOREIGN TRADE ORGANIZATIONS ARE SOMETIMES UNWILLING TO MAKE THE NECESSARY EFFORT OR LOWER THE PRICE SUFFICIENTLY. (3) BILATERAL TRADE

BALANCING IS OFTEN SOUGHT BY FOREIGN TRADE ORGANIZATIONS BUT DOES NOT USUALLY ENTER INTO COMPENSATION ARRANGEMENTS. IN MOST CASES IT IS LEFT UP TO THE FOREIGN SUPPLIER TO MARKET LIMITED OFFICIAL USE

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THE ROMANIAN GOODS WHEREEVER HE CAN, SO LONG AS ROMANIA IS "REPAID" IN THAT FOREIGNERS CURRENCY. THUS THE BALANCE IS IN CURRENCY, NOT TRADE. (COMPANIES USUALLY FIND COMPENSATION ARRANGEMENTS SO BURDENSOME THAT THEY RAISE THE HARD CURRENCY PRICES OF THEIR SALES TO ROMANIA, DEFEATING THIS OBJECTIVE AT LEAST PARTIALLY.) (4-6). IT IS OUR IMPRESSION THAT ROMANIAN OBJECTIVES OF SELF-SUFFICIENT PRODUCTION, CONTINUED FLOW OF TECHNOLOGY, AND ECONOMIES OF SCALE ARE DESIGNED INTO PROJECTS BEFORE THE QUESTION OF COMPENSATION ARRANGEMENTS IS RAISED. WHEN COMPENSATION INVOLVES A LONG TERM ARRANGEMENT WITH A FOREIGN SUPPLIER, THESE OBJECTIVES MAY BE COMPATIBLE.

(B) WESTERN COMPANIES. IN THE MOST COMMON TYPES OF COMPENSATION, AMERICAN AND OTHER WESTERN FIRMS ACCEPT ROMANIAN PRODUCTS ONLY BECAUSE THEY ARE OBLIGED TO BY THE COMPETITION IN SELLING. IN ESTABLISHING A JOINT VENTURE OR OTHER LONG-TERM COOPERATIVE PROJECT, THE FOREIGN FIRM MAY SEEK A CHEAPER OR MORE RELIABLE SOURCE OF INDUSTRIAL SUPPLIES. RAW MATERIALS ARE NOT USUALLY EXPORTED FROM ROMANIA, ALTHOUGH INTERMEDIATE INDUSTRIAL PRODUCTS SUCH AS PETROLEUM PRODUCTS, PETROCHEMICALS, AND STEEL HAVE BEEN USED IN SHORT TERM COMPENSATION DEALS. GIVEN ROMANIA'S POLICY OF PROCESSING ITS OWN RAW MATERIALS TO THE HIGHEST LEVEL POSSIBLE BEFORE EXPORTING, SUCH ARRANGEMENTS ARE NOT LIKELY ON A LONG-TERM BASIS. U.S. FIRMS ARE SOMETIMES INTERESTED IN MORE COMPLEX MANUFACTURED ARTICLES (SUCH AS TRACTORS, AUTOMOBILES OR COMPUTER PERIPHERAL EQUIPMENT), ALTHOUGH AS SUGGESTED ABOVE U.S. FIRMS SEEK MAINLY TO PRODUCE SUCH ARTICLES FOR THIRD MARKETS, NOT THE U.S. THE CHOICE BETWEEN A LONG-TERM CONTRACTUAL AGREEMENT AND EQUITY INVESTMENT IN A JOINT VENTURE IN ROMANIA IS MADE IN THE COURSE OF BARGAINING OVER MANY ISSUES, OF WHICH THE QUESTION OF COMPENSATION IN PRODUCTS IS ONLY ONE. CHOICE OF EQUITY INVESTMENT USUALLY DOES IMPLY, HOWEVER, WILLINGNESS OF THE WESTERN FIRM TO EXPORT OVER HALF OF THE PRODUCTION OF THE JOINT VENTURE FROM ROMANIA.

VII. CONSIDERATIONS FOR U.S. FIRMS.

(A) PROJECTS IN ROMANIA, WHETHER OR NOT THEY INVOLVE COMPENSATION ARRANGEMENTS, SELDOM INVOLVE THE PROBLEMS OF SCALE SEEN IN THE SOVIET UNION. IN SOME CASES THE GOR LIMITED OFFICIAL USE

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PRESSES FOR PROJECTS LARGER THAN U.S. FIRMS BELIEVE SUITABLE FOR THE WORLD MARKET, BUT IN ANY CASE ROMANIA'S DOMESTIC MARKET IS QUITE MODEST BY U.S. STANDARDS. U.S. FIRMS COMPETING IN ROMANIA ARE LARGE ENOUGH TO UNDERTAKE VIRTUALLY ALL PROJECTS THEY CONSIDER REALISTIC; IN A FEW CASES, SUCH AS A STEEL MILL OR A PETROCHEMICAL COMPLEX, THEY HAVE TO FORM CONSORTIA. MARKETING OF GOODS RECEIVED IN COMPENSATION IS EVEN LESS LIKELY TO BE AFFECTED BY THE SIZE OF THE FIRM THAN BY THE FIRM'S ESTIMATE OF WORLD MARKET CONDITIONS.

(B) CURRENT ASSETS VERSUS LONG-TERM INCOME. IN THE FIRST TWO TYPES OF COMPENSATION, BARTER AND PAYMENT IN UNRELATED PRODUCTS, THE QUESTION OF ASSETS VERSUS INCOME IS NOT A MAJOR FACTOR SO LONG AS THE FIRM HAS A REASONABLE CASH FLOW. THE DECISION TO GO INTO PROJECTS WHICH WILL BE PAID (AT LEAST IN PART) OUT OF PRODUCTION WILL DEPEND ON THE FIRM'S LONGER RUN STRATEGY; IF THE FIRM IS SEEKING ADDITIONAL PRODUCTION FACILITIES, THERE IS OF COURSE NO CONFLICT. PROJECTS DO APPEAR TO TAKE LONGER IN ROMANIA THAN IN THE WEST, ESPECIALLY DURING NEGOTIATIONS AND BREAKDOWNS IN THE DECISION MAKING PROCESS. ON THE OTHER HAND THEY ARE LESS LIKELY TO BE DELAYED BY CYCLICAL FORECASTS OR LOCAL NON-GOVERNMENTAL OPPOSITION.

(C) AND (D) VALUE AND TYPES OF GOODS RECEIVED. AGAIN, THESE ISSUES DEPEND UPON THE TYPE OF COMPENSATION INVOLVED, AND WHETHER ACCEPTANCE OF COMPENSATION IS A RELUCTANT CONCESSION OR A DELIBERATE OBJECT. ROMANIA WOULD LIKE, OF COURSE, TO ELIMINATE ITS SURPLUSES OF SUBSTANDARD GOODS, AND TO ESTABLISH

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NEW MARKETS FOR HIGH QUALITY FINISHED GOODS. EMBASSY WOULD EXPECT THAT BOTH TYPES OF COMPENSATION WILL CONTINUE TO BE IMPORTANT: WE DO NOT EXPECT RAPID IMPROVEMENTS IN THE PLANNING SYSTEM, AND WE HAVE SEEN CASES IN WHICH FOREIGN PARTNERS CAN HELP ROMANIA PRODUCE COMPETITIVE FINISHED GOODS. WHEN U.S. FIRMS SEEK ITEMS IN SHORT SUPPLY ON A SHORT TERM BASIS, THEY USUALLY CAN NOT GET THEM AS COMPENSATION FOR EXPORTS TO ROMANIA. WHERE MORE THAN ONE FOREIGN TRADE ORGANIZATION OR MINISTRY IS INVOLVED, IT BECOMES EVEN MORE DIFFICULT TO DO SO.

(E) RELATIONSHIP TO LEVEL OF WESTERN ECONOMIC ACTIVITY. THE RECENT RECESSION CREATED DIFFICULTY FOR AT LEAST TWO AMERICAN FIRMS MARKETING PRODUCTS OF THEIR PROJECTS IN ROMANIA. WE SEE LITTLE DIFFERENCE BETWEEN THE EFFECT OF BUSINESS CYCLES
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ON FIRMS' PROJECTS IN THE HARD-CURRENCY TRADE SECTOR OF ROMANIA AND THEIR OPERATIONS ELSEWHERE IN THE WESTERN WORLD. GOR OFFICIALS IN ECONOMIC POLICY POSITIONS NOW SEEM TO BE WELL AWARE THAT THIS IS AN INEVITABLE RESULT OF ROMANIA'S ORIENTATION OF OVER HALF ITS TRADE TO HARD CURRENCY MARKETS.

VIII. GOVERNMENT FINANCING.

(A) EXIMBANK AND COMPENSATION ARRANGEMENTS. MOSCOW'S COMMENTS AND CRITERIA FOR EXIMBANK PARTICIPATION GENERALLY APPLY IN THE CASE OF ROMANIA. WE WOULD STRESS, AS WE HAVE IN THE PAST, THAT EXIMBANK POLICIES NOT BE BASED PURELY ON THE STRUCTURE OF A GIVEN PROJECT, BUT RATHER ON THE PRACTICAL, COMPETITIVE ALTERNATIVES. FOR EXAMPLE, ONE PROJECT IS UNDER PRELIMINARY CONSIDERATION BY A U.S. FIRM HERE FOR PRODUCTION OF INDUSTRIAL MATERIALS FOR THE U.S. MARKET; IN THE ABSENCE OF EXIMBANK AND/OR OPIC FINANCING, IT MIGHT BE LOGICAL FOR THE FIRM TO OBTAIN ALL OF THE CAPITAL EQUIPMENT NECESSARY FROM

BRITAIN, WITH BRITISH OFFICIAL FINANCING, WHICH WOULD PERMIT THE PROJECT TO EXPORT MAXIMUM QUANTITIES TO THE U.S. MORE FREQUENTLY WE SEE CASES IN WHICH BUYING BACK A SMALL PROPORTION OF A PROJECT'S EVENTUAL OUTPUT HAS BECOME AN ESSENTIAL ELEMENT OF THE WESTERN FIRM'S OFFER TO SELL CAPITAL GOODS HERE.

(B) OTHER WESTERN GOVERNMENTS' POLICIES TOWARD COMPENSATION ARRANGEMENTS. WE ARE NOT AWARE OF ANY INHIBITIONS ON OFFICIAL FINANCING GENERATED BY COMPENSATION ARRANGEMENTS. MOST WEST EUROPEAN FIRMS AND THEIR EMBASSIES HERE LOOK UPON COMPENSATION AS A NECESSARY EVIL IN DOING BUSINESS IN ROMANIA. WITH THE POSSIBLE EXCEPTION OF ITALIAN FIRMS, MOST SELLERS OF CAPITAL GOODS AVOID COMPENSATION IN PRODUCTS WHENEVER THE COMPETITIVE SITUATION PERMITS THEM, BUT HAVE BECOME EXPERT IN UNLOADING UNWANTED PRODUCTS WHEN THEY HAVE TO, USUALLY THROUGH OTHER FIRMS.

IX. RELATION OF COMPENSATION ARRANGEMENTS TO GATT.

(A) COMPENSATION ARRANGEMENTS HAVE HELPED ROMANIA'S TRANSITION FROM A CEMA TRADING COUNTRY TO AN INTERNATIONALLY TRADING COUNTRY. WHILE ROMANIA MAY USE THE CRUTCH OF COMPENSATION LONGER THAN IS REALLY NECESSARY, IT CONTAINS AN ECONOMIC LIMITED OFFICIAL USE

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INCENTIVE FOR ROMANIA TO BEGIN MARKETING MORE OF ITS OWN PRODUCTION.

(B) LONG-TERM BILATERALISM VERSUS MULTILATERALISM. WE DO NOT FIND THAT COMPENSATION ARRANGEMENTS PRODUCE ONLY BILATERAL TRADE; THE GOODS MAY GENERALLY BE SOLD ANYWHERE.

(C) ALTHOUGH COMPENSATION DEALS MAY BE CONTRARY TO THE SPIRIT OF FREE TRADE, IN THE LONG RUN WE WOULD EXPECT THE TRADING SPIRIT TO UNDERMINE COMPENSATION ARRANGEMENTS, EXCEPT IN THOSE CASES IN WHICH FOREIGN FIRMS HAVE AN EQUITY INVESTMENT AND A ROLE IN MANAGEMENT. ROMANIAN OFFICIALS ARE ALERT TO NEW, COMPETITIVE OFFERS FOR THEIR GOODS.

(D) TRADE DISTORTIONS. SO LONG AS WESTERN COMPANIES ARE FREE TO INVEST IN, TRADE WITH OR IGNORE THIS MARKET, WE DO NOT ANTICIPATE SIGNIFICANT TRADE DISTORTION EXCEPT WHEN TRADE MAY BE BLOCKED BY UNAVAILABLE FINANCING OR OTHER DISCRIMINATORY RESTRICTIONS. THE INCREASING LONG-TERM INVOLVEMENT OF WESTERN FIRMS WITH EXPORT COMMITMENTS IN ROMANIA DRAWS ROMANIA INTO, NOT AWAY FROM, THE WESTERN TRADING SYSTEM, HELPING GOV OFFICIALS TO LEARN HOW TO MANUFACTURE AND SELL FOR HARD CURRENCY.

X. POTENTIAL PROBLEMS. ACTIVE AMERICAN EXPORT FIRMS ARE

LEARNING TO COME TO TERMS WITH, AND EVEN PROFIT FROM, COMPENSATION ARRANGEMENTS. WE DO NOT HAVE MUCH CONTACT HERE WITH LABOR, CONGRESSIONAL OR OTHER PUBLIC ATTITUDES ON THIS ISSUE. WE WOULD HOPE THIS STUDY COULD PROVIDE A BASIS FOR OUTLINING TO INTERESTED PARTIES THE FACTS OF LIFE IN EASTERN EUROPE AND THE EXTENT TO WHICH THE U.S. AND OTHER WORLD-TRADING ECONOMIES CAN BENEFIT FROM THEM.

XI. POLICY GUIDELINES. EMBASSY STRONGLY SUPPORTS A PRAGMATIC RATHER THAN A DOCTRINAIRE APPROACH TO COMPENSATION ARRANGEMENTS, AS EXIMBANK SHOWED IN ITS HANDLING OF THE ROLLWAY BEARING CASE IN LATE 1975. ECONOMIC/COMMERCIAL OFFICERS HERE ARE CAUTIONING AMERICAN FIRMS THAT COMPENSATION ARRANGEMENTS COULD AFFECT THE AVAILABILITY OF EXIMBANK FINANCING, AND SEE NO HARM IN CONTINUING TO DO SO. WE RECOGNIZE THAT EXIMBANK CAN HARDLY FINANCE RUNAWAY PLANTS OR NEW PRODUCTION FACILITIES LIMITED OFFICIAL USE

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WHICH COULD BE BUILT IN THE U.S. IF SATISFACTORY FINANCING WERE AVAILABLE, AS ITALY APPEARS TO BE DOING IN THE SOVIET UNION (MOSCOW 1106), BUT THERE ARE MANY MORE CASES IN WHICH THE ONLY DECISIVE ISSUE IS WHERE THE CAPITAL EQUIPMENT WILL BE BOUGHT--AND IN THESE CASES WE WOULD HOPE FOR CONTINUED STRONG SUPPORT BY EXIMBANK FOR U.S. EXPORTER. BARNES

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